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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1956

No. 492

CITY AND COUNTY OF SAN FRANCISCO, a municipal corporation,
Petitioner,

vs.

NATIONAL DISTILLERS PRODUCTS CORPORATION, a corporation,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
to the District Court of Appeal, State of California,
First Appellate District, Division Two.

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PERKAU-WALSH PRINTING CO., SAN FRANCISCO

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to the District Court of Appeal, State of California, First Appellate District, Division Two.

The City and County of San Francisco, petitioner herein, prays respectfully that this Court issue a writ of certiorari to review the decision and judgment of the District Court of Appeal, State of California, First Appellate District, Division Two, entered in the above entitled case on May 21, 1956.

JURISDICTION.

The judgment of the District Court of Appeal, State of California, First Appellate District, Division Two, was filed and entered on May 21, 1956. A petition for hearing in the Supreme Court of the State of California was timely filed on June 29, 1956, which petition for hearing in the Supreme Court of the State of California was denied by order dated July 18, 1956. (Appendix C, hereto *infra* p. xix).

The jurisdiction of this Court is invoked under 28 U.S.C. Section 1257(3).

OPINION BELOW.

The opinion of the District Court of Appeal, State of California, First Appellate District, Division Two, appears in Appendix B, hereto *infra* pp. vi-xviii, and is reported in 141 Advance California Appellate Reports 719.

QUESTIONS PRESENTED.

The District Court of Appeal, State of California, First Appellate District, Division Two, has construed Sections 311, 309(a) and (b) and 313(d) of the Tariff Act of 1930, as amended (19 U.S.C. §§ 1311, 1309(a) and (b) and 1313(d), respectively), granting an exemption from internal revenue tax to articles manufactured of materials subject to internal revenue tax and eventually intended for exportation or for use as

ships' stores, to be an exercise of the Congressional power over foreign commerce under Article I, Section 8, Clause 3 of the United States Constitution, and has declared personal property taxes of the State of California levied pursuant to Section 201 of the Revenue and Taxation Code of the State of California on said articles to be an interference with the federal regulation of foreign commerce and has ordered a refund of said taxes. It has been the contention of petitioner that the grant of exemption by the sections of the Tariff Act of 1930, as amended, set forth above from internal revenue taxes was an exercise of the taxing power of Congress and not the power over foreign commerce, and that therefore the personal property taxes of the State of California were validly levied.

The questions presented are:

1. Whether the grant of exemption from internal revenue tax of articles manufactured from materials subject to internal revenue tax when intended for exportation or for use as ships' stores by Section 311, 309(a) and (b) and 313(d) of the Tariff Act of 1930, as amended, is an exercise of the Congressional power over foreign commerce pursuant to Article I, Section 8, Clause 3 of the United States Constitution or an exercise of the taxing power of Congress pursuant to Article I, Section 8, Clause 1 of the United States Constitution.

2. Whether the grant of an exemption from internal revenue tax by Congress of articles manufactured of materials subject to internal revenue tax and intended for exportation or for use as ships' stores

precludes the exercise by a State of its taxing power over such articles from the moment of the commencement of production of said articles and before such articles become exports or enter the export stream.

STATUTES.

The statutory provisions involved are Sections 311, 309(a) and (b) and 313(d) of the Tariff Act of 1930, as amended (19 U.S.C. §§ 1311, 1309(a) and (b) and 1313(d)), and also Section 201 of the Revenue and Taxation Code of the State of California. These statutes are printed in Appendix A, *infra*.

STATEMENT OF THE CASE.

The Assessor of the City and County of San Francisco levied a nondiscriminatory ad valorem personal property tax pursuant to Section 201 of the Revenue and Taxation Code of the State of California on certain types of liquor owned by respondent, which liquor was situated in the City and County of San Francisco on the tax day of the year 1952, to wit, the first Monday of March. Some of this liquor had been in California since 1947. None of the liquor was at the time the taxes were levied sold or consigned, but was held by respondent to fill orders which might in the future be received. This liquor fell into three classes.

1. Liquor Manufactured in Class 6, United States Customs Bonded Warehouse, and Bottled.

Of the liquor taxed by the Assessor on tax day, 2,076 cases consisted of liquor manufactured in a United States Customs Bonded Warehouse, Class 6, at Baltimore, Maryland, as allowed by federal statute (19 U.S.C. 1311), and then transported to the City and County of San Francisco where it was stored in a Class 3 Customs Bonded Warehouse on tax day. This liquor was 86 or 86.8 proof and was not bottled for domestic use. After the manufacture and bottling of said liquor in the Class 6 warehouse at Baltimore, the liquor was transported to San Francisco upon a bonded common carrier and upon its arrival at San Francisco was stored in a Class 3 customs warehouse under a customs bond conditioned upon exportation. A substantial amount of the liquor in question was still in the warehouse at the time of trial of the said action. Some of the liquor was sold to a local ship chandlery firm, which firm thereafter at various dates sold the said liquor in lots of one or two cases to various ships to be used as ships' stores; some for ships operating between the United States and the Hawaiian Islands, some for ships in the intercoastal trade, and one case was sold to a fishing vessel operating in the local waters in and about the City and County of San Francisco.

2. Liquor Bottled in Internal Revenue Bond.

Of the liquor taxed by the Assessor on tax day 1952, 1,208 cases were manufactured in an Internal Revenue distillery and transferred to and bottled in Baltimore,

Maryland. It was 86 proof and the labels on the bottles were marked "Bottled in Bond for Export" and the cases were marked "For Export from United States of America." The liquor was moved to San Francisco by bonded carrier and it was covered by bonds conditioned upon exportation or use for ships' stores.

3. 5,281 Cases on Which Internal Revenue Taxes Had Been Paid Subject to Drawback.

Of the liquor taxed by the Assessor on tax day 1952, 5,281 cases consisted of liquor upon which internal revenue taxes had been paid but upon which the taxes would be refunded to the respondent upon proof of export or of use for ships' stores consisting of a duly executed landing certificate at a foreign port. This liquor was covered by a bond conditioned upon the exportation of said liquor or the use of said liquor on vessels or aircraft as supplies. These bottles were labeled "For Export" and the cases carried the stamp "Bottled for Export U.S.A." The liquor was moved to San Francisco by common carrier and was held at South End Warehouse in San Francisco on tax day. Some of the drawback liquor was taken into the warehouse on June 28, 1948; part of this lot was exported on May 25, 1953, approximately five years later, indicating that that particular liquor had been in the warehouse for approximately five years; the balance thereof was still in the warehouse on September 1, 1953, indicating that that particular liquor was in the warehouse in the State of California more than five years. Some of the liquor was taken into the warehouse as

early as June 17, 1947 and was not taken out of the warehouse until July 21, 1952, more than five years later.

The trial Court concluded that the instant situation was governed by the United States Supreme Court case of *McGoldrick v. Gulf Oil Corp.* (1939), 309 U.S. 414, and in its conclusions of law stated that the liquor in question "constituted items in foreign commerce over which the federal government has exercised its power of regulation and control to the end that such distilled spirits may be sold or otherwise disposed of for transportation to destinations in foreign countries or sold for use as supplies for specified vessels of the United States free of the burden of domestic taxation." The trial Court ordered the taxes refunded.

Petitioner appealed to the District Court of Appeal, State of California, which Court affirmed the judgment of the trial Court and again concluded that the instant situation was governed by the United States Supreme Court case of *McGoldrick v. Gulf Oil Corp.*, supra.

REASONS FOR ALLOWANCE OF THE WRIT.

The District Court of Appeal, State of California, First Appellate District, has decided an important question of federal law which has not been, but should be, settled by this Court, in that said Court has ruled that the grant of an exemption from internal revenue taxes upon an article manufactured of materials sub-

ject to internal revenue taxes levied solely under the taxing power of the United States Constitution is an exercise not of the taxing power of Congress but of the distinct power to regulate foreign commerce under the United States Constitution (Article I, Section 8, Clause 3), and in so deciding has removed from the taxing power of the State merchandise of domestic origin and manufacture which is not in commerce at the time the taxing power of the State is attempted to be exercised by the State.

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1. **THE GRANT OF AN EXEMPTION FROM INTERNAL REVENUE TAX TO LIQUOR TO BE EXPORTED OR USED AS SHIPS' STORES IS AN EXERCISE OF THE TAXING POWER AND NOT OF THE POWER OVER FOREIGN COMMERCE.**

(A) Levy of Internal Revenue Taxes Is Solely an Exercise of the Taxing Power.

That the levying of internal revenue taxes is an exercise solely and exclusively of the taxing power of Congress cannot be questioned.

See:

License Tax Cases, 5 Wall. 462;
Plumley v. Massachusetts, 155 U. S. 461;
South Carolina v. United States, 199 U. S. 437;
Ohio v. Helvering, 292 U. S. 368.

Similar internal revenue taxes on other products have been held to be levied under the taxing power of the Federal Government.

Felsenheld v. United States (tobacco), 186 U. S. 126;
In re Kollock (oleomargarine), 165 U. S. 526;

United States v. Doremus (drugs), 249 U. S. 86;

Sonzinsky v. United States (firearms), 300 U. S. 506.

(B) The Grant of an Exemption From Internal Revenue Taxes Levied Under the Taxing Power Must Likewise Be Held to Be an Exercise of the Taxing Power and of No Other Federal Power.

The District Court of Appeal, State of California, First Appellate District, Division Two, in the instant case, arrived at the anomalous conclusion that the grant of an exemption from internal revenue taxes admittedly levied under the taxing power of Congress was an exercise not of the taxing power of Congress but of the power over foreign commerce.

Congress has in the past on occasion taxed some articles and exempted others from taxation, which acts of Congress have always been construed to be an exercise of its taxing power.

See:

Western Electric Power Co. v. United States, 336 U. S. 176 (involving a statute taxing electricity sold for domestic or commercial consumption but not taxing electricity sold for industrial consumption);

In re Kollock, 165 U. S. 526 (sustaining the validity of a statute levying a tax of two cents on yellow oleomargarine but leaving uncolored oleomargarine exempt from tax).

The Court was led to this erroneous conclusion by two reasons:

1. That the exemption had been granted by a tariff act, to wit, the Tariff Act of 1930, as amended;
2. That the instant case was similar to the holding of this Court in the case of *McGoldrick v. Gulf Oil Corp.,* 309 U. S. 414.

Neither of these reasons is valid.

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2. THE TARIFF ACT OF 1930 IS BOTH AN EXERCISE OF THE TAXING POWER AND THE POWER OVER FOREIGN COMMERCE, AND THE GRANT OF THE EXEMPTION FROM INTERNAL REVENUE TAXES THEREIN IS AN EXERCISE OF THE TAXING POWER.

The Tariff Act of 1930 is entitled "An Act to Provide Revenue, to Regulate Commerce with Foreign Countries, to Encourage Industries of the United States, to Protect American Labor, and for Other Purposes." It will be noted that the first purpose stated in the title quoted above is "to provide revenue" and that the second purpose is "to regulate commerce with foreign countries."

In *McGoldrick v. Gulf Oil Corp.,* supra, at page 428, it was stated:

> "The laying of a duty on imports, although an exercise of the taxing power, is also an exercise of the power to regulate foreign commerce."

There can be no question, therefore, that the Tariff Act of 1930 was an exercise of both the taxing power of Congress and the power over foreign commerce.

The United States Supreme Court has at various times, depending upon the necessity of sustaining action of Congress under the Tariff Acts, stated that a specific act was an exercise of either the power to tax or the power to regulate foreign commerce, whichever would sustain the validity of the Congressional action in question. Thus, in the case of *University of Illinois v. United States,* 259 U. S. 48, where the issue was whether an import duty could be levied on scientific apparatus imported by an instrumentality of the State, the United States Supreme Court concluded that the import duty was levied under the power of Congress to regulate commerce and not under the taxing power, and that, therefore, the import duty was not a tax on the State. Clearly, in dealing with imports, there would be no doubt as to the validity of this conclusion.

However, in the case of *J. W. Hampton, Jr. & Company v. United States,* 276 U. S. 394, the question was presented of the constitutionality of the Tariff Act of 1922, which allowed the President, with the aid of advisers, to determine what the import duty on specific articles should be, with the express purpose of encouraging and protecting domestic manufacturers of the imported article within the United States. Even though the *Hampton* case involved an import duty in a Tariff Act, the constitutionality of that portion of the Tariff Act of 1922 was sustained as an exercise of the taxing power, and not as an exercise of the power to regulate foreign commerce. The Court there recognized that one of the purposes of the Tariff Act there

in question was to secure revenue for the benefit of the general government, and that that purpose was sufficient to sustain the act even though the motive in fixing the rates of duty was to so fix them as to encourage the industries of the United States in competition with producers in other countries. Thus where the impact of the Tariff Act was as to goods of domestic origin not in commerce, the United States Supreme Court could not sustain the validity of the Congressional action under the commerce power, but was forced to rely on the constitutional power to levy taxes. (See also *License Tax Cases,* 5 Wall. 462.)

The United States Supreme Court held the legislation valid under the taxing power notwithstanding the fact that the particular section of the Tariff Act of 1922 involved in the case of *J. W. Hampton Jr. & Co. v. United States,* supra (Section 315(a) and 315(b) of the said Tariff Act) read in part as follows:

> "That in order to regulate the foreign commerce of the United States . . ."

Thus, in spite of the express Congressional declaration that the purpose was to regulate the foreign commerce of the United States, the United States Supreme Court found it necessary in sustaining the particular provisions of the Tariff Act to rely on the constitutional power granted to Congress to levy taxes.

It should be noted that substantially the same provisions of the Tariff Act of 1922 were re-enacted in the Tariff Act of 1930, as Section 326 of the Tariff Act of

1930, the only significant change being deletion from the said section of the phrase:

> "to regulate the foreign commerce of the United States."

The inclusion in the Tariff Act of 1930 of the flexible tariff provisions of the Tariff Act of 1922, the constitutionality of which latter provisions had been sustained in the case of *J. W. Hampton Jr. & Co. v. United States* as an exercise of the taxing power of Congress, establishes beyond question that certain provisions of the Tariff Act of 1930 are an exercise of the taxing power of Congress. Thus it is established that in looking at the Tariff Act of 1930 it is necessary to examine each particular section to ascertain under what constitutional power the said section is enacted. Where, as in the case of the articles of domestic manufacture, there is no commerce involved and the matter is one of exemption from internal revenue taxes levied pursuant to the taxing power of Congress, the only conclusion that can be reached is that the granting of such exemption is an exercise of the taxing power and no other power.

Petitioner's position is that the levy by Congress of internal revenue taxes on liquor is an exercise by Congress of the taxing power, and that the granting of an exemption by Congress from the selfsame internal revenue taxes to liquor for any purpose whatsoever, even if such liquor is to be exported or to be used for ships' stores, is similarly an exercise of the federal

taxing power. This would be so even though the motive might be to encourage commerce.

It has clearly been established that a distinction must be drawn between the power of Congress to take certain actions and the motive which prompts the taking of said actions.

Thus, concededly, where the motive has been to discourage wagering and gambling and to stifle the gambling racket, such action has been sustained under the taxing power, even though the revenue collected was negligible. (*United States v. Kahriger,* 345 U.S. 22.)

Similarly, where the motive has been to prohibit commerce in marijuana, the action has been sustained under the taxing power (*United States v. Sanchez,* 340 U.S. 42), even though the United States Supreme Court conceded that the revenue purpose of the tax was secondary.

Thus, even though it were to be conceded in the instant case that the exemption from tax would have the incidental effect of encouraging economic activity in the tax-exempt liquor and make the said tax-exempt liquor better able to compete in foreign markets, the important factor would be the power pursuant to which the exemption is granted and not the motive which may have prompted the exercise of the power. The power in the instant case was the taxing power, and as the United States Supreme Court stated in the *Hampton* case, supra:

> "The fact that Congress declares that one of its motives in fixing the rates of duty is to so fix them that they shall encourage the industries of this country in competition with producers in other countries in the sales of goods . . . cannot invalidate a revenue act so framed."

The District Court apparently took the position that because the liquor was manufactured under government regulation for eventual export or use as ships' stores, the liquor was therefore at all times, from the moment its production commenced, segregated from the general mass of personal property and not subject to the taxing power of the State. Such segregation, however, was solely to prevent the diversion of the liquor to the domestic market without the payment of tax, and for no other reason. (See *Dunlap v. United States,* 173 U.S. 65.)

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3. THE CONCLUSION OF THE CALIFORNIA COURTS THAT THE INSTANT SITUATION WAS SIMILAR TO THAT IN THE GULF OIL CASE IS ERRONEOUS.

The District Court of Appeal, State of California, First Appellate District, Division Two, held that "The instant case seems to present a situation that is clearly within the rationale of the Gulf Oil case." (141 A.C.A. 719, 723.) In the *Gulf Oil* case this Court concluded that the grant of an exemption under the Tariff Act of 1930 from *import duties,* the levying

of which import duties was recognized to be an exercise of the Congressional power over foreign commerce, was likewise an exercise of the Congressional power over foreign commerce. The Supreme Court of the United States recognized that the imported merchandise was segregated from the mass of goods within the State and that though the crude oil there involved was processed and refined, it at all times retained its status as an **import** and as a consequence was immune as an import from local taxation. This Court particularly relied on the customs regulation which provided that "imported goods in bonded warehouses are exempt from taxation under the general laws of the several States".

The *Gulf Oil* case, therefore, presents the situation of an exemption from an **import** duty levied under the commerce power, the exemption also being held to be an exercise of the same commerce power.

In the instant case, as distinguished from the *Gulf Oil* case, supra, the merchandise in question was solely and exclusively of domestic origin and the internal revenue tax levied on the particular type of merchandise was levied solely and pursuant to the exercise of the federal taxing authority. If Congress levies the internal revenue tax pursuant to the taxing power and thereafter provides for specific exemptions under which articles shall be free from tax, both the levying of the tax and the exemption therefrom are an exercise of the taxing power and of no other power. Thus, for example, Congress granted the privilege to the United States of pur-

chasing supplies imported from foreign countries to the United States duty-free. By Act of Congress this privilege was extended to all articles of domestic production which were subject to a tax under the Internal Revenue Code so that the United States could purchase such articles without the payment of internal revenue tax. (See 26 U.S.C. §3331.) This was an act by Congress pursuant to the taxing power declaring the policy of tax-free purchases by the federal government. (See *United States v. Mullins* (C.C.A. 6, 1902), 119 Fed. 334; 25 U. S. Attorney General's Opinions 449.) Similarly, Congress has allowed exemptions from taxation as to alcohol used domestically for purposes other than beverage purposes. (See *Dunlap v. United States*, 173 U.S. 65.)

It is respectfully submitted that the grant of exemption from internal revenue taxes of the liquor in question was solely and exclusively an exercise of the taxing power of Congress.

CONCLUSION.

The question involved in this controversy is the construction of federal statutes by a State in such a manner as to raise the issue as to (1) whether the statutes as construed are not beyond the power of Congress under Article I, Section 8, Clause 3 of the United States Constitution, and (2) whether statutes as so construed do not unconstitutionally restrict and limit the taxing power of the State over

articles of a domestic nature which are not in foreign commerce.

Petitioner respectfully submits that for the foregoing reasons the petition for a writ of certiorari should be granted.

Dated, San Francisco, California,
October 1, 1956.

Respectfully submitted,

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(Appendices A, B and C Follow.)